UNITED STATES DEPARTMENT OF AGRICULTURE

Bureau of Agricultural Economics

AGRICULTURE AND THE PARITY YARDSTICK

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I am very glad of this chance to discuss the parity principle and its relation to our agricultural program. For I think the parity device as applied to farm prices and agricultural income stands for something that farm people should never surrender.

Farmers and farm organizations have fought for economic equality in terms of parity prices and incomes for two decades. Today, when both the general principle and our current ways of calculating parities are generally accepted, is no time to desert what we have struggled for over all these years. For this reason the current discussions of the parity principle and methods of calculating and measuring parity are especially significant.

Farmers have long felt that their incomes or standards of living are not comparable to the advantages and standards of living enjoyed by the nonagricultural group. And since the Civil War, certainly, farmers have made many efforts to obtain legislation that would give them a more even break. But the roots of our present parity concept lie chiefly in the events of the last World War and in the depression that immediately followed it.

As many of you remember, there was a great deal of interest in the administration of prices during the last World War. Efforts were made to fix the prices received for milk by producers in several milksheds on the basis of a sliding formula tied to some of the more direct costs of production. The price of wheat was actually fixed, and the question of fixing or guaranteeing the price of hogs was freely discussed.

As all of you remember, farm prices rose somewhat faster than other prices during the first few years of the war period, but they also dropped faster and farther than other prices in 1920 and 1921. As a result of this drop in prices there was a great deal of agitation for some form of agricultural relief during 1921 and 1922. Almost without exception, the ideas and devices that were eventually written into the Agricultural Marketing Act of 1929, the Agricultural Adjustment

Act of 1933, the Agricultural Marketing Agreement Act of 1937 and the Agricultural Adjustment Act of 1938 can all be traced back to this general agitation for farm relief that was first started on a Nation-wide scale during 1921 and 1922.

Some of the agricultural organizations and farm journals in the Mid-West were then asking for corn acreage control; groups throughout the country were considering the cooperative approach to controlling agricultural supplies and raising farm prices; and a great many of the farmers and their representatives were in favor of some kind of arrangement that would increase the export movement of our commodities and so shorten supplies in the domestic market.

In 1921 George Peek and Hugh Johnson prepared their brief on "equality for agriculture" that was to serve as a basis of the McNary-Haugen fight from 1924 to 1928. In this brief the need for raising farm income was set forth, and the suggestion was made that sufficient surpluses be diverted from the domestic market to maintain a "fair exchange value" or raise farm prices to the same relative level as existed in the ten years 1906 to 1915.

About this same time George Warren, who was in charge of agricultural economics at Cornell University for so long, came to Washington and worked out the index for farm prices that was presented in U. S. Department of Agriculture Bulletin 999. In developing this first index of prices paid to farmers — or, as the term is now used, of prices received by producers — the prices for the several commodities were indexed on the basis of the sixty months, August 1909 through July 1914.

The reasons for selecting these five years as a base, as I understand it, were:

(1) It was felt that a base prior to the outbreak of the war in 1914 was desirable since it was believed that a reasonably normal relationship existed between the prices of the several commodities and between the returns to the several groups of producers in the period preceding the World War; and

(2) Although prices of the chief agricultural commodities had been collected for December 1 of each year since the Civil War, the collection of prices on a monthly basis was started during 1909, so that monthly estimates of prices received by farmers were not available prior to 1909.

These two reasons, then, very largely determined the base period that is now used in calculating parity prices and parity income — that is, the five years 1910 to 1914.

Warren also compared farm prices with all wholesale prices in order to obtain a rough measure of the purchasing power of farm products.

This comparison led to several conclusions that have since become quite familiar, and there are several sentences in the summary that I should like to read. Specifically:

"Practically nothing that the farmer sells can be exchanged for the usual quantity of other things. It is physically impossible for farmers to absorb the products of factories. Farm prices have dropped much more than wholesale or retail prices of farm products. The low purchasing power of farm products has made it impossible for farmers to buy the normal amount of other things, and has been a contributing cause of unemployment."

The comparison between prices received by farmers and all prices at wholesale was not, of course, an entirely satisfactory comparison. As a result, Dr. O. C. Stine, with the help of others in the Bureau of Agricultural Economics, worked out an index of prices paid by farmers in local markets for goods used in family living and production. This index was first published in 1928. Since that time, the comparison between prices received for the main agricultural commodities and this index of prices paid by farmers has been the generally accepted measure of the parity relationship.

Of course, a great many other ideas and devices for measuring economic equality as between farmers and non-farmers were advanced during this period. But the parity yardstick was finally accepted in 1933 because it measured off what seemed to be a fairly reasonable goal and could itself be definitely measured.

So we have arrived today at a place where the parity principle is an integral part of our agricultural legislation. The original definition is in the Agricultural Adjustment Act of 1933 which declares that it is the policy of Congress, among other things, to "reestablish prices to farmers at a level that will give agricultural commodities a purchasing power with respect to articles that farmers buy, equivalent to the purchasing power of agricultural commodities in the base period. The base period in the case of all agricultural commodites except tobacco shall be the prewar period, August 1909-July 1914. In the case of tobacco, the base period shall be the postwar period, August 1919-July 1929."

While this formula has been amended and re-enacted several times since 1933, it has not been essentially changed except that allowances for interest payments per acre on farm indebtedness secured by real estate, and tax payments per acre on farm real estate have been added to the purchasing power calculations for all commodities for which the base period is 1909-1914, and the base period for Burley and flue-cured tobacco has been shifted to August 1934-July 1939.

Other amendments also are of interest but they supplement rather than change the original formula. Under the Agricultural Marketing

Agreement Act of 1937 the Secretary is directed to consider "the price of feeds, the available supplies of feeds, and other economic conditions which affect market supply and demand" in determining prices for milk and its products in areas where marketing agreements are in effect. Where satisfactory statistics are not available for the earlier 1910-14 base period the Secretary also is allowed to use "the postwar period, August 1919-July 1929, or all that portion thereof for which. . . . the purchasing power of such commodities can be satisfactorily determined from available statistics" for the purposes of marketing agreements and orders under the Act.

And the so-called "Steagall Amendment" of 1941 provides that whenever the Secretary finds it necessary to give special encouragement to the production of any commodity, such funds as are available shall be so used as to support prices for such commodities at "not less than 85 per·centum of the parity or comparable prices therefor" and that "comparable prices. . . shall be determined and used (whenever) the production or consumption of such commodity has so changed . . . as to result in a price out of line with parity prices for basic commodities." That is, comparable prices are to be used where parity prices are not now available, as in the case of soybeans, or where parity as calculated according to the general formula is clearly out of line with prices of the five basic commodities — corn, cotton, wheat, rice, and tobacco — specified in the Agricultural Adjustment Act of 1938.

With this discussion of the general parity formula in mind we may now consider the method by which parity prices are actually calculated. For the major agricultural commodities (and the same general procedure is followed for all commodities) the steps involved are:

(1) A base price for the period 1909-14 is determined. This is done by averaging the prices reported by farmers to the Department of Agriculture for the sixty months beginning August 1909 and ending July 1914. The average price of cotton during this period, for example, was 12.4 cents a pound, while wheat averaged 88.4 cents a bushel.

There are now about 10,000 dealers in agricultural products reporting to the Department the current prices paid to producers. Similarly, approximately 14,000 local merchants servicing the farm population report retail prices in rural areas which are the chief basis of the "prices-paid" series, although some other sources are also used.

(2) An index of prices paid, including taxes on real estate and interest paid, is calculated. This is a laborious but relatively simple task. To begin with, the prices of 86 items used in family living and 88 items used in farm production are collected. These items include clothing; household supplies; food; furniture and furnishings; building materials; automobiles, trucks, tractors, gas, oil, and tires; feed; farm machinery; fertilizer; general equipment and supplies; and seed.

The necessary data on real estate taxes and interest on indebtedness secured by farm real estate are also collected.

In computing the indexes of prices paid for commodities used in living or family maintenance and commodities used in production, the estimated quantity of each commodity used by farmers is used to weight both the prices paid in 1910-1914 and current prices in order to obtain the necessary ratios or indexes of prices paid. The tax and interest data are calculated as rates per acre and converted into index form.

To obtain the final "index of prices paid, interest and taxes," the index of prices paid for commodities used in living is given a weight of 48.6 percent, while the indexes of commodities used in production and interest and taxes per acre are given a weight of 51.4 percent. This procedure gives an overall index of 138 for October 15, 1941, which means that farm commodity prices would need to be 138 percent of the base prices in order to have the same purchasing power as in 1909-1914.

(3) The third step in calculating parity prices is to adjust the base period prices by the index of prices paid, interest, and taxes. That is, the base period prices are multiplied by 1.38 to calculate the parity prices for October 15, 1941. The parity price for cotton, for example, is 1.38 times 12.4 cents or 17.11 cents a pound, and the parity price for wheat is 1.38 times 88.2 cents or 122.0 cents a bushel. These parities compare with actual prices received of 16.55 cents a pound for cotton and 91.0 cents a bushel for wheat as of October 15.

Parity prices, of course, change as the index of prices paid, interest, and taxes change — that is, parity is a relative rather than a fixed price concept.

For several commodities, chiefly fruits and vegetables, which have only recently come into general use or for which earlier data are not available, the base period is August 1919-July 1929, while for Burley and flue-cured tobacco, as I mentioned a moment ago, the base period is August 1934-July 1939. Parity for these commodities is calculated in exactly the same manner as for other commodities, except that allowances for interest and taxes are not included.

Parity prices calculated according to this formula are published every month by the Department in its Price Report, which also carries prices received by farmers on the fifteenth of the month. The index of prices paid, interest, and taxes, it will be noted, does not include any allowance for sums spent for farm labor. Farm wages on October 15 were 165 percent of the pre-war average, and the current parity index would be raised about 3 points if an allowance for wage rates were included. Wages cannot be included without a legislative amendment.

All of us know, of course, that what farmers are really interested in is income rather than prices as such. As a result, the concept of parity income has developed along with the parity price principle. The best current definition of parity income is in the Agricultural Adjustment Act of 1938 which provides that parity income "shall be that per capita net income of individuals on farms from farming operations that bears to the per capita net income of individuals not on farms the same relation as prevailed during the period from August 1909 to July 1914." This definition applies to the net income available to farm families after cash operating costs are paid.

There is also an implied definition of the gross parity income in Section 303 of the same Act which provides that such funds as are available for price adjustment payments shall be divided among the several basic commodities in proportion to the amount by which each fails to reach the parity income level. For this purpose, parity income has been considered as equivalent to a normal year's domestic consumption and exports of each of the basic commodities times the parity price for the particular season concerned.

There is, I think, general agreement that the parity income is a more rational and equitable approach than is the parity price approach. But the difficulties of determining net incomes available to farm families are considerable; and after this net income is determined there is still the problem of how to apportion it among the several commodities or groups of farmers; and, after this is done, there remains the further problem of what volume of production to use in translating this income into prices that would correspond to parity prices as currently calculated.

Because of these difficulties, we are still using the much simpler parity price approach, although we all hope, I think, eventually to make better use of the parity income approach. Over the long run, it seems only reasonable to appraise our efforts to obtain parity prices in terms of whether or not farmers are actually getting a reasonable or equitable income.

So much for background and method. I want to turn now to the current discussion of the parity yardstick. There are two facts chiefly responsible for most of this interest. First, it so happens that the current draft of the so-called "Price Control Bill" provides, among other things, that no ceilings shall be fixed on the price of farm products at less than 110 percent of the parity price, or the market equivalent of the parity price of agricultural commodities as determined and published by the Secretary of Agriculture; and second, it so happens that the average of all agricultural prices reached the parity level in September of this year for the first time since 1920.

Quite naturally, these facts have stimulated a great deal of interest and discussion, especially within the agricultural field.

Some statisticians would like to see our current methods revised in order to give a somewhat more modern listing and weighting to the commodities involved. Such a revision, however, would certainly change the current indexes by only a very few points and would not mean a great deal to either the farmers or consumers concerned. At the other extreme, there are some individuals and groups who would like to see the method of calculating parity prices so altered as to result in much higher prices than those that are currently being calculated and published. And finally, there are many people who believe that the current methods of determining parity prices and incomes could be measurably improved, or who have formulas of their own that they believe would be better than the current formula, and who would like to see these changes adopted in view of the increasing importance of the parity concept.

Before I discuss some of the suggestions that are now being advanced it might be well to say just a word as to what parity prices do and do not stand for. The parity principle is simply an exchange ratio between prices paid by farmers and prices received. It applies only to those items for which the farmer pays cash and for which prices and rates can be rather easily determined, and to those items that the farmer sells for which prices can be easily determined.

The current parity formula does not attempt to measure cost of production in any of the usually accepted senses in which that term is used. Nor does the current parity formula endeavor to give farm and non-farm families an equal standard of living. Instead, so far as it applies to standards of living, it is devised to give farm families an income that has the same relative purchasing power when compared with the incomes of non-farm families as existed in the base period 1910-1914.

There are, it might be noted, several distinct advantages that attach to the current method. To begin with, it is generally accepted among a surprising number of people -- among farmers, consumers, administrative officials of the Government and legislators. This is an advantage that cannot be brushed aside or easily overlooked. After all, a method that has developed through almost two decades of controversy has proved its merit. There should be a strong case against it, before a suggestion that it be materially changed is really in order. Second, agricultural prices, as a whole were at a relatively higher level as compared with nonagricultural prices during the five years preceding World War I than at any other time since the short war period, 1916 through 1918. This means that efforts to raise parity prices must either lead toward different base periods for different commodities or to a shift toward a substantially different method. And third, statistics for determining parity prices as they are now calculated are fairly easily available and, for the most part, are reasonably adequate. Some of the proposals now being discussed would either require statistics that are not now available, or would involve the use

of statistics and methods that are none too logical. I am not saying this in an effort to prove that agricultural prices and farm returns were satisfactory in 1910-1914, but only to indicate some of the factors that must be considered if a shift is seriously proposed.

There are, of course, any number of proposals for shifting the whole concept and method of calculation. Perhps the best way to consider these proposals is to outline certain classes of approaches rather than to try to consider any specific proposal as such. There is always a tendency for the suggestions developed by different individuals and different groups to fall within a relatively small number of classes, even though each suggestion does have its own identifying differences and does become associated with some different group or background.

One series of current suggestions proposes that the present parity method be replaced by a cost of production approach. As I have already indicated, this is one of the oldest suggested ways for measuring equality or fair returns for agriculture. So far, the cost of production proposals have always led to differences when the particular methods of calculating costs are discussed. That is, as an abstract proposal, the cost-of-production concept seems logical and is easily argued. But as a concrete proposal, it raises so many questions of judgment with respect to values to be placed on the labor of the farmer and his family and on farm land and equipment, and profits to be allowed, that it has generally been passed over whenever the effort was to work out a practical or administrable approach.

A second series of suggestions proposes that the comparisons between farm and non-farm prices be shifted to some other basis, or that some other index be substituted for the current index of prices paid. For the most part, these suggestions would take specially computed indexes for a commodity or type of farming, or some other economic index that would give a higher parity level than is provided by the index now being used. Proposals that special indexes be used for each of the important agricultural commodities, or for each of the important agricultural regions or types of farming, have considerable merit. As you all realize, it can very well be argued that a national index of prices paid, interest, and taxes is not the best index to use in comparing prices for milk with the cash costs of dairy farmers in the Northeast or the Mid-West, or in the milkshed of some particular city like San Francisco or Detroit. But the statistical task of determining a whole series of regional or commodity indexes, and the arguments that would be raised along the route, make this approach difficult. And proposals simply to shift the basis for comparison away from the index of prices paid to some more favorable general index are, of course, always open to question, unless the new index better measures prices paid by farmers than does the current index.

Another series of suggestions would require that the current parity prices for all commodities be redetermined in such a manner as

to modernize the relations between prices received for each of the several commodities and yet leave the average level of parity prices unchanged. This proposal, you understand, would say to consumers that the average parity price level for all commodities would remain unchanged, but in order to distribute more equitably the costs and benefits of the farm program, the parity prices for each of the individual commodities will be recalculated in such a way that all of them will be equally close to or equally far below the parity level. It is usually suggested that the price relations prevailing during 1934-1939 be used. Considered as an abstract suggestion, this proposal has merit. But you all will recognize that, practically, it would mean that parity prices of about one-half of the commodities would be raised above the present parity level and the parity prices for the other half would be lowered. The one-half of the farmers whose parity prices were raised would, of course, not seriously object, but the other half of the farmers would be almost certain to raise a big question, if not a big howl.

And finally, there is a series of suggestions that assumes that farmers should obtain the same absolute income in dollars per capita or per family as non-farmers, or at least a considerably greater relative income per capita than is provided by the definitions of agricultural prices and income carried in current farm legislation. Some of these suggestions ask that a weight of as much as 50 percent be given to wage indexes of industrial and other non-farm workers, while others assume that parity income should give farmers an absolute dollar income equal to one-half or two-thirds or the same total dollar income as is received per capita by the nonagricultural group. The proposal to use a wage index along with the prices paid index has certain drawbacks. As far as prices paid by farmers are concerned, the wages of industrial labor are necessarily included in the prices paid for processed food or farm machinery or cotton clothing, or whatever else is bought. As a result, this aspect of the wage situation is already measured in the prices paid index. On the other hand, if it is argued that the wage indexes are used to measure the income that farmers should have available for family living and for savings, it would seem more appropriate to use average income per capita of the entire nonagricultural group than to use industrial wage rates, or even weekly or monthly earnings of industrial workers, since the parity concept or principle should measure the differences between farmers and non-farmers, rather than differences between farmers and some special classes or groups in the nonagricultural field. As for the proposals to give farmers some specified or relative income, they often fall in much the same class as the cost of production proposals, as well as bring up the question of whether dollar incomes of farmers and non-farmers can be directly compared.

But all of this discussion is good, whatever we may think of any specific proposal. We want the best agricultural program that can be worked out, and we all want our program and the standards upon which it

is based generally understood. This is necessary if the farmers, their representatives, and the general public are to have the confidence that is indispensable to the success and continuation of the program itself. And since it is the farmers and the general public, working through the Congress, who make the final decisions, I am glad that so many people are aware of the importance of the parity principle and are trying to learn more about it.

So far as the Department of Agriculture is concerned, we are making every effort to explain our statistics and our methods to congressional committees, to farmers and farm organizations, to administrators in other agencies, and to representatives of the general public itself. Certainly we feel that the farmers and farm organizations cannot afford to put themselves in the position of asking for changes in methods of determining parity that would appear to have as their chief justification an attempt to obtain extraordinary profits out of the present defense situation. Even if successful in the short run, such proposals would certainly shake public confidence in the entire farm program, and would only add to the already too plentiful material for encouraging inflation.

For the good of the farm program itself we must see to it that such changes as are adopted are reasonable and logical.

In conclusion, I should like to point out that the welfare of farm people is dependent upon many other things besides parity prices and the methods by which they are calculated. Parity income and parity prices are important, of course, but they serve only as standards against which to measure prices and incomes received from commercial sales by all farmers. There are many other ways by which farm standards of living can be improved. The whole parity price and income concept, for example, has little bearing on the incomes and standards of living of that 50 percent of the farm population who operate very small farms or who work as farm laborers and who account for not more than 15 or 20 percent of our total farm production. There are plenty of other problems in the farm field; and although we want to work out the best parity price and income measures that can be devised, we must never forget that these are, after all, only a part of our whole farm program. Farm standards of living must be raised, and all classes of farmers must benefit in this process. Meanwhile, we cannot forget that we are now in the midst of a world-wide struggle for self-preservation, and that agriculture's first emphasis should be on what it can contribute to our defense effort rather than on how much self-advantage can be derived from it.